

Message Text

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TO SECSTATE WASHDC IMMEDIATE 6725
ALL EC CAPITALS

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TAGS: EEC, EFIN, ECON
SUBJECT: EC FINANCE COUNCIL, MAY 22, 1978

REF: (A) BRUSSELS 7529; (B) COPENHAGEN 2345;
(C) COPENHAGEN 2400; (D) BRUSSELS 3398

1. SUMMARY: DURING THEIR MAY 22 COUNCIL MEETING, THE EC
FINANCE MINISTERS HELD AN INITIAL SUBSTANTIVE DISCUSSION
OF THE COPENHAGEN EUROPEAN COUNCIL'S CONCLUSIONS CONCERN-
ING COMMUNITY GROWTH OBJECTIVES FOR MID-1979 AND POSSIBLE
COMMUNITY ACTIONS IN THE MONETARY SECTOR (REFS A, B, AND
C). MOST MEMBER STATES EXPRESSED AGREEMENT WITH THE EC
COMMISSION'S ASSESSMENT THAT THE 4.5 PERCENT COMMUNITY
GROWTH TARGET FOR JULY 1979 CANNOT BE ATTAINED WITHOUT
COORDINATED ACTION BY THE MEMBER STATES, INCLUDING IN-
CREASED PUBLIC SPENDING WHEREVER POSSIBLE. THE FRG,
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HOWEVER, CONTINUED TO INSIST THAT THE COMMUNITY SHOULD
NOT TIE ITSELF TO SPECIFIC GROWTH TARGETS AND THAT ANY
COMMON ECONOMIC STRATEGY CONSIDERED BY THE UPCOMING
BREMEN AND BONN SUMMITS SHOULD NOT BE BASED UPON GROWTH
FACTORS ALONE. WITH GERMAN ACQUIESCENCE, THE MINISTERS
DID, NEVERTHELESS, AGREE THAT THE COMMISSION SHOULD
PREPARE RECOMMENDATIONS ON INDIVIDUAL MEMBER STATE CON-

TRIBUTIONS TO COLLECTIVE EC ACTION, FOR CONSIDERATION BY THE JUNE 19 FINANCE COUNCIL. THE MINISTERS ALSO ASKED THE MONETARY COMMITTEE TO SUBMIT TO THE JUNE COUNCIL ITS RECOMMENDATIONS ON POSSIBLE ALTERNATIVE MODELS FOR EC COOPERATION IN THE MONETARY FIELD. UNDER A SEPARATE AGENDA ITEM, THE COUNCIL APPROVED AND FORWARDED TO THE EUROPEAN PARLIAMENT THE REVISED DRAFT TEXT OF A DECISION TO ESTABLISH A NEW COMMUNITY LOAN INSTRUMENT (ORTOLI FACILITY). END SUMMARY

2. COMMON ECONOMIC STRATEGY:

MINISTERIAL DEBATE WAS PREFACED BY A REPORT FROM COMMISSION VICE PRESIDENT ORTOLI, WARNING THAT, IN THE ABSENCE OF STRONG COORDINATED ACTION, THE 4.5 PERCENT JULY 1979 GROWTH TARGET WOULD NOT BE ACHIEVABLE AND THAT COMMUNITY GROWTH OVER THE COMING YEAR WOULD IN FACT AMOUNT TO BETWEEN 2.5 AND 3 PERCENT. IN A CONFIDENTIAL PAPER SUBMITTED TO THE COUNCIL, THE COMMISSION INDICATED THAT CURRENT CALCULATIONS SHOW THAT INCREASED PUBLIC SPENDING ON THE ORDER OF 0.8 PERCENT OF COMMUNITY GNP WOULD HAVE A MULTIPLIER EFFECT OF 2 BY THE END OF THE FOURTH QUARTER OF 1978 (ASSUMING ACTION BY JAPAN AND OTHER EUROPEAN COUNTRIES), LEADING TO ADDITIONAL EC GROWTH OF 1.7 PERCENT AND KEEPING ALIVE THE POSSIBILITY THAT THE 4.5 PERCENT TARGET MIGHT BE ACHIEVED NEXT YEAR.

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3. THE COMMISSION PAPER EMPHASIZES THAT THERE IS NO SINGLE AND NON-CONTROVERSIAL METHOD FOR DETERMINING CAPACITY FOR REFLATIONARY ACTION BY INDIVIDUAL MEMBER STATES, AND PARTICULARLY FOR WEIGHING AGAINST EACH OTHER THE DIFFERENT CRITERIA WHICH MUST BE CONSIDERED IN ANY SUCH ANALYSIS (E.G. LABOR MARKET, INFLATION, FINANCIAL POLICY, BALANCE OF PAYMENTS). HOWEVER, THE COMMISSION HAS ESTABLISHED THE FOLLOWING RANKING OF THE MEMBER STATES IN DESCENDING ORDER OF THEIR CAPACITY TO TAKE ADDITIONAL REFLATIONARY ACTION: GERMANY, NETHERLANDS, LUXEMBOURG, BELGIUM, FRANCE, UNITED KINGDOM, DENMARK, IRELAND, AND ITALY. THE PAPER OFFERS THE FOLLOWING JUSTIFICATIONS FOR ITS VIEWS ON EACH COUNTRY:

(A) GERMANY:

DOMESTIC POLICY MEASURES TAKEN LAST FALL WERE FOLLOWED BY STRONG ECONOMIC RECOVERY, BUT ECONOMIC ACTIVITY DECLINED IN THE FIRST PART OF 1978 AND FORECASTS THROUGH 1979 CALL FOR NO IMPROVEMENT; IT SHOULD THEREFORE BE SUGGESTED THAT EXISTING MEASURES WILL NOT PRODUCE A DURABLE RECOVERY OR A RETURN TO STRONG GROWTH. IN ADDITION, GERMAN ECONOMIC PROSPECTS ARE NOT STRONG ENOUGH TO JUSTIFY

VIGOROUS EXPANSION IN NEIGHBORING COUNTRIES. THE ESSENTIAL OBSTACLE TO A
D
DITIONAL GERMAN MEASURES LIES IN CONSTITU-
TIONAL AND FINANCIAL POLICY RESERVATIONS AGAINST LARGE
BUDGET DEFICITS; THE ONLY REAL SOLUTION TO THE PROBLEM
OF DEFICITS IS JOINT ACTION LEADING TO A DURABLE UPSWING
IN ALL OF THE COMMUNITY, THEREBY PROVIDING NEW IMPETUS
TO THE GERMAN DOMESTIC ECONOMY. THIS SOLUTION WOULD
REQUIRE TEMPORARY BUDGET DEFICITS IN GERMANY AND OTHER
MEMBER STATES, BUT GOVERNMENTS COULD EXPECT TO RECOUP
THESE LOSSES AS INCREASED TAX REVENUES RESULT FROM EX-
PANSION.

(B) NETHERLANDS:
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PROSPECTS FOR REAL ECONOMIC GROWTH ARE EQUALLY POOR
IN THE NETHERLANDS, ALTHOUGH THE MONETARY AND FINANCIAL

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SITUATIONS ARE RELATIVELY FAVORABLE. SOME DANGERS ARE ALREADY IN VIEW: GAS EXPORTS WILL DECLINE AT THE BEGINNING OF THE 1980.S AND THE BUSINESS SECTOR IS ALREADY WORRIED ABOUT COMPETITIVENESS. THE NETHERLANDS THEREFORE HAVE LATITUDE FOR GROWTH WHICH SHOULD BE EXPLOITED AS PART OF JOINT COMMUNITY ACTION; UNCOORDINATED ACTION BY THE NETHERLANDS ALONE WOULD NOT BE EFFECTIVE.

(C) BELGIUM AND LUXEMBOURG:

BOTH DIFFER LITTLE FROM THE NETHERLANDS. ECONOMIC ACTIVITY IS SOMEWHAT STRONGER IN BELGIUM, BUT BELGIAN STATE FINANCES ARE MORE HEAVILY STRAINED AND THE BELGIAN FRANC HAD TO BE SUPPOED LAST YEAR. ON THE OTHER HAND THE BELGIAN INFLATION RATE IS CONSIDERABLY LOWER. THOUGH PERHAPS WITH A SLIGHT DELAY, THE BELGIAN ECONOMY COULD MAKE CONSIDERABLE GAINS THROUGH AN EXPANSIONARY POLICY, IN THE EVENT OF A GENERAL EUROPEAN RECOVERY. LUXEMBOURG.S LIMITED OFFICIAL USE

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STATE FINANCES ARE NOT NEARLY SO STRAINED AS BELGIUM.S, BUT STEEL INDUSTRY PROBLEMS CARRY COMPARABLY MORE WEIGHT.

(D) FRANCE:

FRANCE LIES IN THE MIDDLE GROUND. THE FIGHT AGAINST INFLATION HAS MADE SOME PROGRESS BUT HAS NOT YET BEEN DECISIVE. THE LATEST ADJUSTMENT OF PUBLIC UTILITIES RATES HAS HAD AS ITS FIRST EFFECT AN INCREASE IN CONSUMER PRICES. NEVERTHELESS, GROWTH PROSPECTS ARE IMPROVED, AND THE FRENCH ECONOMY IS DYNAMIC AND COMPETITIVE. GOVERNMENT DEFICITS HAVE BEEN KEPT WITHIN RELATIVELY NARROW BOUNDS. FRANCE HAS SOME LATITUDE FOR EXPANSION IF OTHER MEMBER STATES ACT ENERGETICALLY, BUT NOT OTHERWISE.

(E) UNITED KINGDOM:

THE APRIL 1978 BUDGET HAS PRACTICALLY EXHAUSTED THE UK.S LATITUDE FOR MANEUVER. THE POUND IS AGAIN WEAKER AND BALANCE OF PAYMENTS VULNERABLE. PRODUCTION SEEMS TO BE RESPONDING MORE WEAKLY THAN CONSUMPTION AND DEMAND. THE INFLATION RATE HAS BEEN IMPRESSIVELY REDUCED BUT THE REPERCUSSIONS OF THE APRIL BUDGET, PARTICULARLY ON THE RELATIONSHIP BETWEEN REAL GROWTH AND INFLATION, LARGELY DEPEND ON WHETHER THE UK SUCCEEDS IN STRENGTHENING ITS POSITION IN INTERNATIONAL ECONOMIC ACTIVITY. THIS LATTER FACTOR SHOULD ALSO BE A PREREQUISITE TO ANY ADDITIONAL LIMITED EXPANSION MEASURES THE UK MIGHT POSSIBLY TAKE THIS SUMMER.

(F) DENMARK:

GROWTH PROSPECTS ARE POOR, AND DENMARK IS CURRENTLY PURSUING A RESTRICTED COURSE, REFLECTING ITS EXTRA-LIMITED OFFICIAL USE

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ORDINARILY STRAINED MONETARY AND FINANCIAL SITUATIONS. DANISH ECONOMIC POLICIES COULD ONLY BE CHANGED IF CONSIDERABLY STRONGER GROWTH WERE CERTAIN.

(G) IRELAND:

THE 1978 BUDGET WAS HIGHLY EXPANSIONARY, AND THE CURRENT HIGH GROWTH RATE LIES AT THE UPPER LIMIT OF THE JUSTIFIABLE. THIS CURRENT GROWTH WILL PROBABLY NOT CONTINUE IF THE EC ECONOMY STAYS ON ITS PRESENT COURSE.

(H) ITALY:

NO LATITUDE IS LEFT AT ALL. IT IS AN OPEN QUESTION WHETHER THE LATEST STRONG IMPULSE TO THE ECONOMY WILL PROMOTE GROWTH OR JUST DRIVE UP PRICES; THIS DEPENDS TO A GREAT EXTENT ON THE GOVERNMENT AND THE SOCIAL PARTNERS BUT PARTLY, AS WELL (THROUGH BALANCE OF PAYMENTS AND EXCHANGE RATES), ON WHETHER OR NOT THERE IS A EUROPEAN ECONOMIC UPSWING.

3. RECOMMENDATIONS FOR JOINT ACTION:

THE COMMISSION PAPER PROPOSES SEVERAL GENERAL PRINCIPLES FOR JOINT COMMUNITY ACTION:

(A) ALL MEMBER STATES SHOULD ACT WITHIN THE LIMITS OF THE LATITUDE AFFORDED BY THEIR INDIVIDUAL CIRCUMSTANCES (AS DISCUSSED ABOVE); IN SOME CASES, THIS COULD CALL FOR EC FINANCIAL AID.

(B) ALL MEMBER STATES MUST EXPECT TO CHANGE THEIR CURRENT ECONOMIC POLICY POSITIONS (COMMENT: PRESUMABLY TO VARYING DEGREES) IF ANY ESSENTIAL CHANGE IN EC ECONOMIC PROSPECTS IS TO BE EXPECTED.

(C) THE ECONOMIC PACKAGE FOR THE BREMEN AND BONN SUMMITS IN JULY SHOULD CONTAIN A MAXIMUM OF POLICY DECLARATIONS OF INTENT.

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(D) ALTHOUGH DEADLINES FOR LEGISLATION AND IMPLEMENTATION OF ECONOMIC POLICY DECISIONS WILL NECESSARILY EXTEND OVER

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A CERTAIN TIME FRAME, EVERY EFFORT SHOULD BE MADE TO CO-
ORDINATE THEM. THE ECONOMICALLY STRONGER COUNTRIES SHOULD
ACT, SO FAR AS POSSIBLE, IN MID-1978, WHILE THE WEAKER
COUNTRIES MIGHT WAIT UNTIL 1979.

(E) ALL PROPOSALS FOR NEW ACTION BY THE MEMBER STATES
MUST BE INTERDEPENDENT.

4. COUNCIL DISCUSSION:

IN AN ON-THE-RECORD PRESS BRIEFING, UK CHANCELLOR OF THE
EXCHEQUER HEALEY INDICATED THAT ALL MINISTERS BUT FRG
STATE SECRETARY SCHLECHT SUPPORTED THE COMMISSION'S ARGU-
MENTS. HEALEY ALSO SAID THAT SEVERAL MEMBER STATES
INDICATED THEY WOULD TAKE NEW GROWTH MEASURES WITHIN THE
NEXT TWO MONTHS. HEALEY ADDED THAT SCHLECHT MODIFIED HIS
INITIALLY NEGATIVE ATTITUDE AFTER HEARING THE OTHER
MINISTERS SPEAK AND THAT THE GERMANS NOW ACCEPT THE NEED
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FOR MEMBER STATE ACTION ACCORDING TO NATIONAL CIRCUM-

STANCES. POINTING OUT THAT THE COMMISSION PAPER DID NOT INCLUDE NUMERICAL TARGET FOR INCREASES IN GNP OR DEMAND, HEALEY SAID THAT THE COUNCIL HAS ASKED THE COMMISSION TO SPECIFY ITS RECOMMENDATIONS FOR INDIVIDUAL MEMBER STATE CONTRIBUTIONS TO COLLECTIVE COMMUNITY ACTION, FOR CONSIDERATION BY THE MINISTERS AT THEIR JUNE 19 COUNCIL MEETING.

5. AT HIS OWN POST-COUNCIL BACKGROUND PRESS BRIEFING, SCHLECHT SAID THAT HIS ATTITUDE TO THE COMMISSION PAPER HAD CHANGED TO ONE OF "OPTIMISTIC REALISM". HE ALSO EMPHASIZED THE GERMAN VIEW THAT MULTIPLIER EFFECTS WOULD BE AMONG THE MOST IMPORTANT ASPECTS OF A COMMON ACTION PROGRAM. IN A SEPARATE BRIEFING, A GERMAN SPOKESMAN EMPHASIZED THAT THE FRG OPPOSES NARROWING CONSIDERATION OF COMMON ACTION TO A DISCUSSION OF GROWTH ALONE, EXCLUDING SUCH OTHER FACTORS AS TRADE AND NORTH/SOUTH ISSUES.

6. MONETARY ACTION:

HEALEY TOLD REPORTERS THAT THE COUNCIL RECEIVED A SHORT REPORT FROM MONETARY COMMITTEE CHAIRMAN VAN YPERSELE, WHICH EMPHASIZED THE COMMITTEE'S CONCLUSION THAT THE COMMUNITY SHOULD AVOID TWO SETS OF EXTREMES IN PURSUING NEW MONETARY SECTOR INITIATIVES. IT SHOULD NOT ASSUME THAT MONETARY STABILITY IS IMPOSSIBLE WITHOUT CONVERGENCE OF ECONOMIC PERFORMANCE, NOR SHOULD IT TOTALLY EXCLUDE CONVERGENCE AS A FACTOR CONTRIBUTING TO MONETARY STABILITY. THE COMMUNITY SHOULD NOT ASSUME IT CAN DO NOTHING TO ACHIEVE MONETARY STABILITY EXCEPT AS PART OF WIDER CO-OPERATION, INCLUDING US COMMITMENTS ON THE DOLLAR, NOR SHOULD IT ACT IN TOTAL INDIFFERENCE TO THE DOLLAR.

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HEALEY SAID THAT THE MONETARY COMMITTEE HAS BEEN ASKED TO SUBMIT TO THE JUNE 19 COUNCIL "TWO OR THREE MODELS" FOR EC COOPERATION IN THE CURRENCY FIELD, INCLUDING ANALYSES OF THE ADVANTAGES AND DISADVANTAGES FOR THE STRONGER AND WEAKER CURRENCIES UNDER EACH MODEL AND OF THE POSSIBLE ROLES OF VARIOUS INSTRUMENTS, SUCH AS POOLING OF RESERVES, AN EXPANDED ROLE FOR THE EUROPEAN UNIT OF ACCOUNT, AND MONETARY TARGETS.

7. COMMUNITY LENDING FACILITY:

THE COUNCIL REACHED AGREEMENT ON A REVISED VERSION OF THE DRAFT DECISION TO CREATE A NEW COMMUNITY LENDING FACILITY (REF D). THE NEW DRAFT WILL BE FORWARDED TO THE EUROPEAN PARLIAMENT IN ACCORDANCE WITH PROVISIONS OF THE CONCILIATION PROCEDURE.

8. OTHER BUSINESS:

THE COUNCIL AGREED TO DISCUSS ADJUSTMENT OF COMMUNITY LOAN
MECHANISMS AT THE JUNE 19 COUNCIL. IT ALSO TOOK NOTE OF
THE COMMISSION'S INTENTION TO SUBMIT IN THE NEAR FUTURE
A PROPOSAL REGARDING DELAYED APPLICATION OF THE SIXTH VAT
DIRECTIVE. HINTON

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